

Memorandum 95-75

Homestead Exemption: Proceeds Exemption

At the November meeting, the Commission approved the recommendation on the *Homestead Exemption*, subject to working out a procedure for controlling the use of proceeds from sale of a homestead during the six-month exemption period in a manner that does not impose special burdens on escrow agents or other third persons. This procedure is intended to preserve the proceeds for use in the purchase of another home in California and not to provide a large cash fund for the use of the debtor for some other purpose.

Originally, the staff suggested that the proceeds be held in escrow for the six-month exemption period or until a new home is purchased, whichever is earlier. The Commission decided, however, that title companies and escrow agents should not be burdened by this new procedure. The staff has been conferring with the California Land Title Association, but as yet we have not gotten CLTA's final input. In view of the impending meeting, the staff believes it is best to proceed without CLTA's input so that the bill can be prepared in time to meet bill introduction deadlines in the 1996 legislative session. If any technical problems arise later, the bill can be revised before introduction or amended afterward.

The following draft provides that all homestead proceeds, whether from a voluntary or involuntary sale, should be restricted to the purchase of another home within six months of the time proceeds are payable to the debtor. The Commission should consider whether the restriction should apply only as to voluntary sales. If a debtor's house burns down or is destroyed in an earthquake or flood, should the debtor be able to use the insurance proceeds in the amount of the homestead exemption (\$50,000-\$100,000) for any purpose? Existing law provides no restriction on the use of proceeds from an involuntary sale through execution or condemnation or of insurance for damage or destruction of the home. However, in view of the sizable exemption provided for homesteads, it seems a fair trade-off that the proceeds be restricted to the purpose of providing

a home for the debtor and the debtor's family. Note, however, that this limitation would not apply in bankruptcy.

The draft also restricts the proceeds exemption to the purchase of another home in California. To provide otherwise would add potentially significant burdens to the creditor's attempt to enforce the money judgment and invite debtors to attempt to leave the state to defeat the judgment lien. While some may think it is simply part of the game to defeat judgment liens, the policy of the law should be to encourage benign liens of record, such as the judgment lien, which do not generally disrupt debtors' possession of their homes. If too many limitations and costs are imposed on judgment liens, creditors may be compelled to use execution and force the debtor out of the dwelling.

The following draft shows the changes the Commission has already approved, as well as newly proposed revisions to control the proceeds exemption in subdivisions (b)(1) (changing "are actually received by" to "become payable to"), (e), and (f):

Code Civ. Proc. § 704.720 (amended). Homestead exemption

SEC. 4. Section 704.720 of the Code of Civil Procedure is amended to read:

704.720. (a) A homestead is exempt from enforcement of a money judgment as provided in this article and is exempt from sale under this division to the extent provided in Section 704.800.

(b) The proceeds from a disposition of a homestead are exempt for the purpose of purchasing another homestead in this state under the following conditions:

(1) If a homestead is sold under this division or is damaged or destroyed or is acquired for public use, the proceeds of sale or of insurance or other indemnification for damage or destruction of the homestead or the proceeds received as compensation for a homestead acquired for public use are exempt in the amount of the homestead exemption provided in Section 704.730. ~~The proceeds are exempt for a period of six months after the time date the proceeds are actually received by~~ become payable to the judgment debtor, except that, if a homestead exemption is applied to other property of the judgment debtor or the judgment debtor's spouse during that period, the proceeds thereafter are not exempt.

(2) If a homestead is voluntarily sold, or otherwise sold in a manner not described in paragraph (1), the proceeds of sale are exempt in the amount of the homestead exemption provided in Section 704.730 for a period of six months after the date of the sale.

(3) If a homestead exemption is applied to other property of the judgment debtor or the judgment debtor's spouse during the six-month period provided in paragraph (1) or (2), the proceeds exemption terminates.

(c) If the judgment debtor and spouse of the judgment debtor reside in separate homesteads, only the homestead of one of the spouses is exempt and only the proceeds of the exempt homestead are exempt.

(d) The exemption of proceeds provided in paragraph (2) of subdivision (b) does not apply to the enforcement of a judgment for child, family, or spousal support, unless the judgment debtor obtains an order, on noticed motion, that the proceeds are exempt in all or part. In making this determination, the court shall apply the standards provided in subdivision (c) of Section 703.070.

(e) Unless otherwise agreed by the judgment debtor and judgment creditor, proceeds exempt or claimed to be exempt under this section shall be deposited with the court. At any time during the six-month exemption period, the court shall, on noticed motion of the judgment debtor, make an order applying the proceeds to the purchase of another dwelling in this state. Unless the judgment debtor purchases another dwelling in this state during the six-month exemption period, the court, on noticed motion, shall order the proceeds applied to the satisfaction of the judgment.

(f) The proper court for filing motions under this section is the court where an application for an order of sale of the dwelling would be made under Section 704.750.

Comment. Subdivision (a) of Section 704.720 is revised for clarity and for consistency with other exemption provisions. See, e.g., Sections 703.010, 704.010, 704.020.

Subdivision (b) is amended to adopt as a general rule the exemption for proceeds of voluntary sales under former Section 704.960 (homestead declaration) and to make clear that the purpose of the proceeds exemption is to permit the debtor to attempt to buy another dwelling in California. Subdivision (b)(1) is amended to provide that the six-month exemption period runs from the date when the proceeds become payable to the debtor rather than when the debtor actually receives the proceeds. This revision is necessary to conform with the procedure in subdivision (e) for restricting the judgment debtor's access to the exempt proceeds. Subdivision (b)(3) is generalized from the last clause of former subdivision (b) of this section. See also Section 703.080 (tracing exempt funds).

Subdivision (d) is a new provision which implements the application of the general rule on equitable division of exemptions in Section 703.070 in a situation where the judgment debtor has multiple support obligees. Unlike the general rule, however, subdivision (d) places the burden on the judgment debtor to file the motion and seek the court order.

Subdivision (e) provides a new procedure for restricting the judgment debtor's access to the exempt proceeds, in fulfillment of the purpose of the homestead exemption.

Subdivision (f) specifies the proper court for proceedings under this section.

Revised Background Comment (1982). Subdivision (a) of Section 704.720 supersedes former Civil Code Section 1240 (providing for a declared homestead)

and former Code of Civil Procedure Sections 690.3 and 690.31(a) (providing for a claimed dwelling exemption). Unlike the former provisions, Section 704.720 does not specify the interest that is protected and does not limit the homestead in a leasehold to a long-term lease; any interest sought to be reached by the judgment creditor in the homestead may be entitled to the exemption. The homestead exemption does not apply where a lien on the property other than an enforcement lien is being foreclosed. See Section 703.010.

Subdivision (b)(1) provides an exemption for proceeds of an execution sale of a homestead, for proceeds from insurance or indemnification for the damage or destruction of a homestead, and for an eminent domain award or proceeds of a sale of the homestead for public use. Subdivision (b)(1) supersedes portions of former Civil Code Sections 1256 and 1265 and of former Code of Civil Procedure Sections 690.8 and 690.31(k). The exemption for insurance proceeds was not found in former law. *But see* Houghton v. Lee, 50 Cal. 101, 103 (insurance proceeds for destruction of declared homestead exempt).

Subdivision (c) is new. The spouses may select which of the homesteads is exempt. If the spouses are unable to agree, the court determines which homestead is exempt. See Section 703.110 (application of exemptions to marital property). Note that a married person may, after a decree of legal separation or an interlocutory judgment of dissolution of marriage, be entitled to a homestead in his or her own right, and this right is not affected by subdivision (c). See Section 704.710(d) (“spouse” defined) & Comment.

Respectfully submitted,

Stan Ulrich
Assistant Executive Secretary